

**BLIMPIE OF CALIFORNIA, INC.**

**FINANCIAL STATEMENTS  
DECEMBER 31, 2002 AND 2001**

BLIMPIE OF CALIFORNIA, INC.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of  
Blimpie of California, Inc.

We have audited the accompanying balance sheets of BLIMPIE of CALIFORNIA, INC. (a C corporation) as of December 31, 2002 and 2001 and the related statements of income (loss), stockholder's equity (deficit) and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of BLIMPIE of CALIFORNIA, INC. as of December 31, 2002 and 2001, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted the United States of America.

March 3, 2003  
Atlanta, Georgia

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A Summit International Affiliates Certified Public Accountants

BLIMPIE OF CALIFORNIA, INC.  
BALANCE SHEETS  
DECEMBER 31,

ASSETS

	<u>2002</u>	<u>2001</u>
<u>Current assets</u>		
Cash	\$ 23,257	\$ 14,509
Accounts receivable, net of allowance for doubtful accounts of \$30,000 for 2002 and \$30,000 for 2001	<u>48,934</u>	<u>92,749</u>
Total current assets	<u>72,191</u>	<u>107,258</u>
<u>Equipment</u> , at cost, net of accumulated depreciation of \$14,522 for 2002 and \$14,052 for 2001	<u>792</u>	<u>1,262</u>
<u>Other assets</u>		
Advances to affiliates	210,798	210,798
Advances to officers	259,743	199,059
License agreement, net of accumulated amortization of \$87,916 for 2002 and \$82,916 for 2001	<u>12,084</u>	<u>17,084</u>
Total other assets	<u>482,625</u>	<u>426,941</u>
	<u>\$ 555,608</u>	<u>\$ 535,461</u>

LIABILITIES AND STOCKHOLDER'S EQUITY

<u>Current liabilities</u>		
Lines of credit	\$ 82,012	\$ 88,579
Accounts payable and accrued expenses	167,434	242,604
Due to advertising fund	<u>218,586</u>	<u>124,226</u>
Total current liabilities	<u>468,032</u>	<u>455,409</u>
<u>Deferred income</u> , net of deferred expense of \$21,500	<u>36,500</u>	<u>60,500</u>
<u>Stockholder's equity</u>		
Common stock, no par value: 10,000 shares authorized, 640 shares issued and outstanding	640	640
Paid-in capital	83,627	83,627
Accumulated deficit	<u>(33,191)</u>	<u>(64,715)</u>
Total stockholders' equity	<u>51,076</u>	<u>19,552</u>
	<u>\$ 555,608</u>	<u>\$ 535,461</u>

See auditors' report and accompanying notes

BLIMPIE OF CALIFORNIA, INC.  
 STATEMENTS OF INCOME (LOSS)  
 FOR THE YEARS ENDED DECEMBER 31,

	<u>2002</u>	<u>2001</u>
<u>Revenue</u>		
Continuing franchise fees	\$ 417,179	\$ 471,845
Initial franchise fees	24,000	5,000
Other	<u>40,647</u>	<u>53,557</u>
Total income	<u>481,826</u>	<u>530,402</u>
 <u>Expenses</u>		
Continuing licensing fees	169,442	189,041
General and administrative expense	250,839	348,199
Rent	<u>30,021</u>	<u>51,562</u>
Total expenses	<u>450,302</u>	<u>588,802</u>
Income (loss) before taxes	31,524	(58,400)
Income taxes	<u>0</u>	<u>0</u>
Net income (loss)	<u>\$ 31,524</u>	<u>\$ (58,400)</u>

See auditors' report and accompanying notes

BLIMPIE OF CALIFORNIA, INC.  
STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)  
FOR THE YEARS ENDED DECEMBER 31, 2002 AND 2001

	Common Stock		Paid-in Capital	Equity (Deficit)	Advances to Total
	Shares	Amount			
Balances, January 1, 2001	640	\$ 640	\$ 83,627	\$ (6,315)	\$ 77,952
Net loss	-	-	-	(58,400)	(58,400)
Balances, December 31, 2001	-	640	83,627	(64,715)	19,552
Net income	-	-	-	31,524	31,524
Balances, December 31, 2002	<u>640</u>	<u>\$ 640</u>	<u>\$ 83,627</u>	<u>\$ (33,191)</u>	<u>\$ 51,076</u>

See auditors' report and accompanying notes

BLIMPIE OF CALIFORNIA, INC.  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31,

Increase (Decrease) In Cash

	<u>2002</u>	<u>2001</u>
<u>Cash flows from operating activities</u>		
Net income (loss)	\$ 31,524	\$ (58,400)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Provision for bad debts	30,000	30,000
Depreciation and amortization	5,470	6,119
Changes in operating assets and liabilities		
(Increase)Decrease in accounts receivable	13,815	(87,941)
Decrease in prepaids and other current assets	0	2,078
Increase(Decrease) in accounts payable and accrued expenses	(75,170)	81,899
Increase(Decrease) in due to advertising fund	94,360	(84)
Increase(Decrease) in deferred income	<u>(24,000)</u>	<u>18,000</u>
Net cash provided(used) by operating activities	<u>75,999</u>	<u>(8,329)</u>
<u>Cash flows from investing activities</u>		
Repayment of officer loans	0	23,075
Loans to officers	0	(100,894)
Repayment of advances to affiliates	0	44,000
Advances to affiliates	<u>(60,684)</u>	<u>(16,261)</u>
Net cash used by investing activities	<u>(60,684)</u>	<u>(50,080)</u>
<u>Cash flows from financing activities</u>		
Net (payments)proceeds on/from short-term borrowings	(6,567)	21,519
Contributions to capital	<u>0</u>	<u>0</u>
Net cash provided(used) by financing activities	<u>(6,567)</u>	<u>21,519</u>
Net increase(decrease) in cash	8,748	(36,890)
Cash, beginning	<u>14,509</u>	<u>51,399</u>
Cash, ending	<u>\$ 23,257</u>	<u>\$ 14,509</u>

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid during the years for interest	\$ 3,483	\$ 3,617
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See auditors' report and accompanying notes



BLIMPIE OF CALIFORNIA, INC.  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31,

Increase (Decrease) In Cash

See auditors' report and accompanying notes

BLIMPIE OF CALIFORNIA, INC.  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2002 AND 2001

**Note A**

**Organization and Summary of Significant Accounting Policies**

Blimpie of California, Inc., a California Corporation, (the Company), markets Blimpie restaurant franchises in California, as an area franchisor. All of the Company's business is dependent upon the economic conditions within the state of California.

Cash and cash equivalents:

For purposes of the statement of cash flows, all unrestricted investment instruments with original maturities of three months or less are deemed cash equivalents. The Company had no cash equivalents at December 31, 2002 and 2001.

Revenue recognition:

The Company reports franchise fees as income when all material services or conditions relating to the sale of a franchise have been substantially performed or satisfied in accordance with the terms of the franchise agreement. The Company reports direct costs related to franchise fees when the income is recognized.

Continuing franchise fee income and license expense are based on a percentage of the gross revenues earned by operating restaurant units as defined in the franchise agreements.

Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Depreciation:

Depreciation of equipment is computed principally on an accelerated method over five years based on the estimated useful lives of the assets.

License agreement:

The license agreement cost is being amortized on a straight-line basis over a 20-year period.

Basis of presentation:

Certain 2001 balances have been reclassified to conform to 2002 presentation.

BLIMPIE OF CALIFORNIA, INC.  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2002 AND 2001

**Note B**  
**Franchising Operations**

License agreement:

The Company has a license agreement with Blimpie International, Inc. ("BII"), for the exclusive right to use the "Blimpie" trademark and technical information (recipes, methods, processes, etc.) in California. Terms of the license agreement provide that the Company is charged an initial franchise fee for each California location licensed and a continuing license fee of 2.5% of the gross revenues of the restaurants in operation. The term of the license agreement is for 99 years beginning July 1984 with renewal options as defined in the license agreement.

The license agreement, originally signed in 1984, was amended on April 30, 1992. The amended license agreement requires the Company to license not less than three Blimpie locations annually for the next 15 years. The obligation is cumulative and the Company will be credited in succeeding years for the number of Blimpie locations licensed in excess of three in any given year. Should the Company not comply with this requirement, the license agreement shall be deemed automatically terminated and cancelled. However, the agreement shall remain as to those Blimpie Restaurants developed or in the process of development with respect to any franchise or subfranchise executed between the Company and any third party as of the date of default.

Significant commitments and obligations:

In accordance with the terms of each franchisee's agreement, the Company is obligated to provide the following supervision assistance and services: layout, training and pre-opening assistance, operations manual, continuing assistance, as specified in the Uniform Franchise Offering Circular, advertising and promotion, supplies, and pricing.

Franchise ownership changes:

For the year ended December 31, 2002, franchise ownership changes are summarized as follows:

Number of franchises in operation as of December 31, 2001	47
Number of franchises opened during the year	3
Number of franchises closed during the year	<u>(3)</u>
Number of franchises in operation at December 31, 2002	<u><u>47</u></u>

**Note C**  
**Related Party Transactions**

Advances to affiliates:

At December 31, 2002 and 2001, advances to affiliates with common ownership for working capital purposes totaled \$210,798 for 2002 and \$210,798 for 2001. Interest earned on advances to affiliates totaled \$0 for 2002.

BLIMPIE OF CALIFORNIA, INC.  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2002 AND 2001

**Note C**

**Related Party Transactions - Cont'd**

Advances to officers:

As of December 31, 2002 and 2001, the Company was owed \$259,743 and \$199,059, respectively, for advances made to two of the Company's officers. Interest was charged at rates of 6% to 7% per annum. Interest earned on advances to officers amounted to \$0 and \$0 for the years ended December 31, 2002 and 2001, respectively.

**Note D**

**Lines of Credit**

The Company has entered into credit agreements with two banks under which it may borrow up to \$100,000 under revolving lines of credit. Current borrowings bear interest from 7.25% to 9.27% per annum. The stockholder has guaranteed borrowings under the lines of credit. During the years ended December 31, 2002 and 2001, interest incurred totaled \$3,483 and \$3,617, respectively.

**Note E**

**Due to Advertising Fund**

The Company receives a percentage of each franchisee's sales to be placed in an advertising co-operative fund, at the Company's sole discretion as described in the franchise agreements. At December 31, 2002 and 2001, the Company owed \$218,586 and \$124,226, respectively, to the advertising co-operative fund.

**Note F**

**Commitments**

During the years ended December 31, 2002 and 2001, the Company incurred rent expense of \$30,021 and \$51,562, respectively.

**Note G**

**Related Party**

Effective January 24, 2002, the Company's principal shareholder purchased a majority interest in Blimpie International, Inc.